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No. 03-917

In The Supreme Court of the United States

RONALD CLEVELAND, doing business as Lone Star Videotronics; PHOENIX-MERCHANT INVESTMENTS INC., doing business as 49er Video; THE BIG PICTURE VIDEO INC.,

Petitioners,

v.

VIACOM INC.; PARAMOUNT HOME VIDEO, INC.; BUENA VISTA HOME ENTERTAINMENT, INC.; COLUMBIA TRI-STAR HOME VIDEO, INC.; UNIVERSAL STUDIOS HOME VIDEO, INC.; TWENTIETH CENTURY FOX HOME ENTERTAINMENT, INC.; BLOCKBUSTER INC.,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

REPLY IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

DAVID E. WARDEN
Counsel of Record
GEORGE FIBBE
YETTER & WARDEN, L.L.P.
909 Fannin, Suite 3600
Houston, Texas 77010
Tel: 713.632.8000
Fax: 713.632.8002

STEPHEN M. HACKERMAN
HACKERMAN FRANKEL, P.C.
1122 Bissonnet
Houston, Texas 77005
Tel: 713.528.2500
Fax: 713.528.2509

Counsel for Petitioners

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

LIST PURSUANT TO RULE 29.6

The caption of this case contains the names of all the parties to the proceedings in the Fifth Circuit Court of Appeals. Pursuant to Rule 29.6, petitioners state as follows: Neither corporate petitioner Phoenix-Merchant Investments Inc. nor corporate petitioner The Big Picture Video Inc. is the subsidiary of any parent corporation. Further, no publicly held company owns 10% or more of either corporation's stock.

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REASONS FOR GRANTING THE PETITION

In an economy that champions competition, price fixing cannot be tolerated because it undermines the free enterprise system. Indeed, price fixing has been condemned since the Roman Empire,[1] because as Adam Smith, the father of capitalism, observed in 1776: "People of the same trade seldom meet together even for merriment or diversion, but the conversation ends in a conspiracy against the public and in some contrivance to raise prices."[2] Section 1 of the Sherman Act demands the same intolerance today of price fixing conduct.

I. Conspiracy To Fix Prices.

The fundamental proof of conspiracy in this case is:

- It is undisputed that Blockbuster had motive and opportunity to instigate the conspiracy – it was being outcompeted by the independent retailers, and thereafter Blockbuster met with each studio and discussed pricing (Pet. at 4-5);
- It is undisputed that as a result of those meetings Blockbuster got the new favored pricing terms it wanted, and it is uncontested that the plaintiffs' distributors did not (Pet. at 5, App. 51-53);
- It is admitted that the studios' conduct was consciously parallel (Opp. at 14, n. 33) – each studio agreed to the Blockbuster terms with Blockbuster but did not agree to such terms with plaintiffs' distributors (Pet. at 9-10);

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[1] Article 59(2) of the Constitution of Emperor Zeno of 483 A.D. prohibited price fixing in relation to clothes, fishes, sea-urchins and other goods, the sanction for violation being perpetual exile. *See* Codex Justinianus, Book 4, Title 59, § 2, p. 186 (Weidmann, 1954).

[2] Adam Smith, An Inquiry Into the Nature and Cause of the Wealth of Nations 55 (Great Books ed. 1952) (1776), cited in *United States v. Taubman*, 297 F.3d 161, 164 (2d Cir. 2002).

- It is admitted that entering agreements on Blockbuster terms with plaintiffs' distributors would have been in the best individual economic interests of the studios – in fact, the studios each say they attempted to do so but the distributors would not agree (Pet. at 9-10); and
- Direct evidence from the distributors contradicted the defendants' assertion – the two largest distributors both repeatedly requested the Blockbuster terms. (Pet. at 10-11, n. 13)

There is nothing ambiguous about any of this evidence – by any measure it meets the requirements of presenting a fact issue as to conspiracy under *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986). Defendants' Brief in Opposition (respondents here) is primarily a suggestion as to how facts in the record might be viewed differently from plaintiffs' construction (Opp. at 3-9, 12-22), but defendants do not, and cannot, refute the fundamental evidence of conspiracy. Defendants' "spin" of the facts is irrelevant at summary adjudication; thus, these facts, construed in plaintiffs' (petitioners here) favor, are all that is needed to defeat JMOL. *Reeves v. Sanderson Plumbing Prod., Inc.*, 530 U.S. 133, 151 (2000).

Defendants' price fixing scheme was not new – it was essentially the same scheme used by J.D. Rockefeller in the 1870s to monopolize the oil industry by fixing prices so that competitors' costs were too high to stay in business.[3] Here, Blockbuster induced the studios to maintain higher videotape acquisition costs for the independent retailers' distributors, thereby driving many independent retailers out of business and allowing Blockbuster to capture their market share. The studios' admissions showed that the

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[3] *See* Elizabeth Granitz and Benjamin Klein, "Monopolization by 'Raising Rivals' Costs': The Standard Oil Case," 39 J. Law & Econ. 1 (1996), cited in *JTC Petroleum Co. v. Piasa Motor Fuels, Inc.*, 190 F.3d 775, 778 (7th Cir. 1999) (Posner, J.).

scheme worked – Blockbuster dramatically increased its market share at the expense of thousands of independent retailers who went out of business because they were denied the favored acquisition terms. (Pet. at 6, App. 53-55, 75-80) This is blatant price fixing at its worst: a conspiracy that amounts to "interference with the setting of price by free market forces is unlawful per se." *United States v. Container Corp. of America,* 393 U.S. 333, 337 (1969); *United States v. Socony-Vacuum Oil Co.,* 310 U.S. 150 (1940).

A. The Legal Issue is Properly Framed.

Respondents pose the issue by describing the court of appeals analysis: "[t]he Fifth Circuit *reviewed all the evidence* in the record and reached the *unremarkable conclusion* that petitioner's so-called pretext evidence was inadequate to defeat judgment as a matter of law." (Opp. at 21, emphasis added) But that is *not* an "unremarkable conclusion" in the face of the direct evidence refuting the proffered business justification. In that context – accepting as we must that the court did consider all the evidence – the result can only be a new legal standard, one in which evidence of a business justification for consciously parallel conduct against self-interest, even if contradicted, trumps evidence that is universally held as a matter of law to permit inference of conspiracy. This is precisely the legal issue posed by petitioners. (Pet. at 24-25)

B. *Matsushita* did not change the Federal Rules.

Respondents' recitation of what *Matsushita* means and how courts are to apply it would encroach on the Federal Rules of Civil Procedure governing summary adjudication. Certainly, *Matsushita* did not do that: it does not impose a special burden on plaintiffs responding to JMOL or summary judgment in antitrust cases, but "demands only that the nonmoving party's inferences be reasonable in order to reach the jury, a requirement that was not invented, but merely articulated, in that decision."

Eastman Kodak Co. v. Image Technical Serv., Inc., 504 U.S. 451, 468 (1992). Rather, the focus of *Matsushita* is on the court's role to filter the permissible inferences that may be drawn from ambiguous circumstantial evidence to prove conspiracy in an antitrust case.

Here the fundamental inference to be considered is whether parallel conduct which is against individual economic self-interest permits an inference of conspiracy. All courts that have considered such conduct in an antitrust setting agree that it does. (Pet. at 9) Thus, the only question is whether there is evidence of such conduct in this record – and indeed there is, comprised of admissions and direct controverting evidence of third parties as set forth above.

The specific conduct complained of in this case is that the studios gave Blockbuster favored videotape acquisition terms that they denied to plaintiffs – clearly anticompetitive behavior.[4] The matter of law for the court is whether that conduct allows inference of conspiracy.[5] Parallel conduct against individual economic self-interest has arisen sufficiently in antitrust litigation that there is no doubt that collusion is a proper inference from such conduct. (Pet. at 9) The question of fact for the jury is

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[4] While revenue sharing in theory could be pro-competitive and lawful, it is illegal to conspire to deny those acquisition terms to a certain segment of the retail market (the independents' distributors) and thus force customers to limit their choices of retailers from whom they can rent videotapes. This is precisely the kind of conduct this Court has said "is not to be tolerated." *Klors, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207, 213 (1959).

[5] The court's role under *Matsushita* is analogous to a court's role in a contract case to interpret the contract. E. Farnsworth, Contracts § 7.14, at 516 (1982) (citing *Brown & Co. v. M'Gran*, 39 U.S. (14 Pet.) 479, 493 (1840) (Story, J.) (It is "certainly true, as a general rule that the interpretation of written instruments properly belongs to the court and not to the jury.")). Likewise, in a patent case it is the court's role to "construe the claims." *Markman v. Westview Instruments, Inc.*, 517 U.S. 370 (1996).

whether the conspiracy actually occurred – here defendants admit the accused conduct resulted in plaintiffs not getting the same deals as Blockbuster, but they offer an innocent business justification as to why it occurred. Because the proffered business justifications are controverted by the direct evidence of third parties, JMOL could not be granted unless a new rule of law is implemented. That is precisely what the Fifth Circuit imposed: it is now not enough that the plaintiff controvert defendants' business justification evidence, it must completely disprove all evidence of business justification to avoid JMOL. This is contrary to *Matsushita* and *Reeves,* as well as the Federal Rules of Civil Procedure.

C. There Is Confusion About *Matsushita* and the Fifth Circuit Is in Conflict.

Although *Matsushita* is considered the standard for determining summary adjudication in price fixing conspiracy cases, numerous courts, commentators, and practitioners find the proper application of *Matsushita* to be the source of widespread confusion in antitrust law.[6] Despite the Court's intention in *Matsushita* to clarify, rather than enlarge, the rule announced in *Monsanto Co. v. Spray-Rite Serv. Corp.,* 465 U.S. 752 (1984), the four dissenting

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[6] *See, e.g., Merck-Medco Managed Care, L.L.C. v. Rite-Aid Corp.*, 201 F.3d 436, 1999 WL 691840 at *5 (4th Cir. 1999) ("The standards for summary judgment and the limits on inferences in antitrust lawsuits are often quoted but not universally agreed upon."); Richard A. Posner, Antitrust Law, 2d ed. 2001, at 99-100 (calling the "tends to exclude the possibility of independent action" requirement adopted by *Matsushita* "unfortunate dictum" that "handicap[s]" the "development of this area of the law."); Areeda & Hovenkamp, *cited in* Pet. at 21 n.17 (cautioning against being misled by the "tends to exclude" language); Daniel R. Shulman, *Proof of Conspiracy in Antitrust Cases & the Oligopoly Problem*, 4 Sedona Conf. L. J. 1, 15 (2003) ("The law now . . . is a mess. Courts cannot agree on what the relevant plus factors are, and their relative weights.").

justices thought it "only muddies the waters."[7] When applying *Matsushita*, some courts of appeals have even derived further tests to simplify or systematize the analysis,[8] while others have hewn closely to each step of *Matsushita's* reasoning, including its emphasis on the plausibility of the economic theory.[9] Within this patchwork of approaches, the point of acute and outcome-determinative confusion that is raised by this case is the proper treatment of defendants' innocent explanations or business justifications for parallel conduct that would otherwise indicate collusion. Few defendants are without such explanations, and the evidentiary burden that courts place on plaintiffs to rebut them – mere scintilla, plausibility, preponderance, clear and convincing, overwhelming – should at least approach uniformity among the circuits.

The Fifth Circuit's approach establishes a regime in which direct evidence contradicting a business justification is not sufficient to create an issue of fact. This started in *Viazis v. Amer. Ass'n of Orthodontists,* 314 F.3d 758 (5th Cir. 2002), was extended here (Pet. at 23-25), and constitutes a severe departure from general summary adjudication standards,[10] from *Matsushita*, and from other circuits.

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[7] *Matsushita*, 475 U.S. at 599 (White, J., dissenting) ("The Court's opinion today . . . only muddies the waters . . . mak[ing] confusing and inconsistent statements about the appropriate standard for granting summary judgment.").

[8] *See, e.g., Williamson Oil Co., Inc. v. Phillip Morris USA,* 346 F.3d 1287, 1301 (11th Cir. 2003) (describing three-step analysis); *In re Citric Acid Litigation*, 191 F.3d 1090, 1094 (9th Cir. 1999) (setting out two-part burden-shifting test when plaintiffs rely on circumstantial evidence).

[9] *See Petruzzi's IGA Supermarkets, Inc. v. Darling-Delaware Co., Inc.*, 998 F.2d 1224 (3d Cir. 1993); *In re High Fructose Corn Syrup Antitrust Litigation*, 295 F.2d 651 (7th Cir. 2002).

[10] Plaintiffs seek only to bring the Fifth Circuit back within the basic standards for evaluating evidence in all cases. *Cf. Reeves*, 530 U.S. 133, 154 (Ginsburg, J., concurring) ("Under [the] common sense principle [that the jury is entitled to treat a party's dishonesty about a

(Continued on following page)

Petitioners' position is that the courts should not foist on plaintiffs an evidentiary burden so great that evidence of business justification *that is controverted* defeats a plaintiff's prima facie conspiracy case of consciously parallel conduct against economic interest. Should this Court grant the petition, the issue before it would be what burden defendants must bear with their evidence of business justification; or the other side of the same coin, what burden plaintiffs must bear in sufficiently rebutting business justifications to survive summary adjudication.[11]

According to respondents, *City of Tuscaloosa v. Harcros Chemicals, Inc.*, 158 F.3d 548 (11th Cir. 1999), *Petruzzi's*, 998 F.2d 1224, and *RE/Max International, Inc. v. Realty One, Inc.*, 173 F.3d 995 (6th Cir. 1999), stand for the unremarkable proposition that business justifications that are nonexistent, nonsensical, or logically incredible are not sufficient for defendants to prevail on summary judgment. (Opp. at 23-25) Similarly, respondents characterize *In re Brand Name Prescription Drug Antitrust Litigation*, 123 F.3d 599 (7th Cir. 1997) as holding that "smoking gun" evidence of conspiracy defeats summary judgment regardless of innocent interpretations of conduct. Thus, defendants appear to support the Fifth Circuit's approach that any business justification that is better than nonsensical, and any evidence of conspiracy that is less than a "smoking gun," mandates summary adjudication, even where the business justification is

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material fact as evidence of culpability], evidence suggesting that a defendant accused of illegal discrimination has chosen to give a false explanation for it gives rise to a rational inference that the defendant could be masking its actual, illegal motivation.").

[11] Because the issue presented by this petition concerns the proper evidentiary standard, the Court's opinion might involve examination of some portion of the evidence in this case. This does not, however, counsel against the granting of the petition, as most decisions of this Court addressing evidentiary burdens or adjudication standards and especially in this area *e.g.*, *Matsushita*, 475 U.S. at 577, have required such evaluation.

directly controverted. This position is so extreme as to constitute a split among the circuits.

Between the evidentiary extremes that respondents posit lie most price fixing cases and lies the Fifth Circuit's departure. To explain the Fifth Circuit's result, respondents recite the mantra that plaintiffs' evidence did not "tend to exclude" independent conduct. But this is a non-sequitur that conflates different levels of analysis – "tends to exclude" answers nothing where the question is what evidentiary burden is required to rebut a business justification.

D. Respondents' Deceptions

Respondents misrepresent important facts, including for example:

Opp. at 9, n. 27: Contrary to respondents' assertion, Petitioners are *not* parties to the action in California state court. (Pet. at 6, n. 5)

Opp. at 6, 16: It is inaccurate to state that the Blockbuster deals were "expensive and risky commitments" requiring "increased capital," "additional advertising" and increased "cost-of-goods." In truth, Blockbuster committed to spend with each studio only the amount of money it had historically, but got significantly more videotapes of the best movies, and both Blockbuster and the studios shared in the substantially increased profits. (Pet. at App. 53-55)

Opp. at 15: Contrary to respondents' statements, the largest distributor, David Ingram, repeatedly testified that he and the independent retailers wanted and requested revenue sharing deals on the same terms that Blockbuster got (34 RT 1959, 1966, 1970, 1972-73). This is strong testimony from a man who knew this testimony was adverse to the studios' wishes and admitted he was beholden to the studios for his economic well-being: "I do not have a company if the studios don't wish me to exist, so I do what the studios want us to do." (34 RT 1974)

Opp. at 15: It is misleading to assert that plaintiffs "never asked their distributors for output revenue sharing." The Blockbuster deals were confidential (34 RT 2041; 31 RT 1226), so plaintiffs did not know exactly what to call them, but their testimony is clear: Q: " . . . did you ask these studios to give you the same kind of deal that they were giving Blockbuster?" A: "Yes, I did." (30 RT 751) The major distributors testified that retailers asked for the same deal that Blockbuster had. (Pet. at App. 67-69) All three plaintiffs testified they wanted and could do output revenue sharing. (Pet. at App. 74)

Opp. at 5, 15-16: All the testimony about whether offers of revenue sharing were made or were rejected is self-serving testimony of high level studio executives that is irrelevant to consider for JMOL. *Reeves,* 530 U.S. at 151.

Opp. at 18, n. 47: While the court did not admit the Ingram letters to the studios into evidence, it did allow repeated testimony of the substance and import of the letters, including verbatim quotation from the letters that the Blockbuster deals had created an unfair advantage, that output deals had not been made available to independent retailers, that 615 dealers had been driven out of business in 90 days as a result, and that the playing field was not level. (34 RT 1984-86, 2011, 2015-16, 2018-20, 2023-24, 2026-30)

Opp. at 18-19: Contrary to respondents' assertion, neither Warner, MGM, nor any other studio ever offered plaintiffs' distributors output revenue sharing on terms "identical to" or "more favorable than" the Blockbuster deals. (Pet. at App. 51-53)

For respondents to assert that they have treated "petitioners' factual allegations in the light most favorable to them" (Opp. at 3, n. 2) is disingenuous at best.

II. Robinson-Patman Act – Price Discrimination.

The Fifth Circuit's reliance on *F.T.C. v. Borden*, 383 U.S. 637 (1966), in this case is misplaced. (Pet. at App. 9) The facts of that case had nothing to do with "like terms and conditions" as a prerequisite to Robinson-Patman Act liability, but rather the issue was whether differences in labeling of an identical product could justify price discrimination. This Court found that such differences, even if economically important to the consumer, did not provide cover for price discrimination, i.e., it was not a defense. *Id.* at 640. But the Fifth Circuit interprets that case to justify its conclusion that since Blockbuster and the independent retailers' distributors now purchase on different terms, Robinson-Patman liability could not attach. (Pet. at App. 8-9) This position is absurd. The products being purchased, videotapes of the same movies, were identical, and the terms and conditions under which Blockbuster and the independent retailers' distributors purchased were identical before the discrimination complained of in this case. If the Fifth Circuit is right, then this Court's decision in *Borden* overruled *F.T.C. v. Morton Salt,* 334 U.S. 37 (1948). There is no indication that this Court meant that to occur.

CONCLUSION

It is inadvisable to shackle the law meant to protect the public from price fixing with an evidentiary standard so high as to leave it ineffective. The Fifth Circuit has done so; the Petition for Certiorari should be granted.

Respectfully submitted this 9th day of February, 2004.

DAVID E. WARDEN
Counsel of Record
GEORGE FIBBE
YETTER & WARDEN, L.L.P.
909 Fannin, Suite 3600
Houston, Texas 77010
Tel: 713.632.8000
Fax: 713.632.8002

STEPHEN M. HACKERMAN
HACKERMAN FRANKEL, P.C.
1122 Bissonnet
Houston, Texas 77005
Tel: 713.528.2500
Fax: 713.528.2509

Counsel for Petitioners